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REUTERS/Fayaz Aziz

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Pakistan has long been constrained by inadequate infrastructure, leaving many parts of the country barely connected to commercial centers by road or rail and creating chronic power shortages that hinder the expansion of manufacturing. These woes, on top of Pakistan's geopolitical instability and history of communal violence, have left the economy struggling to match other Asian economies that are developing rapidly.

So when the $62 billion joint-initiative China-Pakistan Economic Corridor(CPEC) was unveiled in 2013, then-Prime Minister Narwaz Sharif hailed it as a gigantic leap forward. Consisting of a series of energy-production and infrastructure projects crossing the whole of Pakistan, the CPEC formed the centerpiece of Chinese President Xi Jinping's $1 trillion "new silk road" (formally, the Belt and Road Initiative). China would provide expertise and loans; Pakistan would be required to repay the debt with substantial interest as the fruits of rising productivity began rolling in.

The Promise

Cheerleaders for CPEC envisioned a host of benefits beyond the expected gains in economic productivity. In particular, they argued that the initiative would narrow Pakistan's regional income gap by connecting impoverished areas including southern Punjab, rural Sindh and most of Baluchistan with commercial hubs. One government report estimated that, all told, CPEC would boost Pakistan's economic growth from 5.8 percent in 2018 to 7 percent by 2023.

This forecast assumed that infrastructure-led development along the lines of Albert Hirschman's unbalanced growth model is realistic in present-day Pakistan. In theory, the rapid expansion in infrastructure would alleviate transport, power and communications bottlenecks that constrained growth, drastically lowering production costs across broad sectors of the economy. It would create a virtuous circle, spurring investment and giving homegrown entrepreneurs a chance to break out.

The Inconvenient Reality

But wishing won't make it happen. And the evidence indicates that infrastructure investment has never triggered much private investment. Indeed, it's the other way 'round: economic growth has spurred infrastructure investment. Even if causality could be reversed, private investment is likely to lag, given Pakistan's political instability — and unfriendly business environment.

Pakistan ranked 131st of 180 countries in the 2018 Heritage House Index of Economic Freedom, placing the country in the index's "mostly unfree" category. That's behind the likes of Papua New Guinea, Haiti and Ghana. Heritage House attributed the country's low ranking to regulatory overreach, corruption and the reality that most Pakistani firms lack access to credit at competitive terms. Also cited: Pakistan's snail-like judicial system and rickety civil service.

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The recent deterioration in Pakistan's macroeconomic situation is a more immediate, and arguably as serious, turn-off for private investors. Since the start of 2017, Pakistan's foreign currency reserves have dropped by half, to less than $10 billion — roughly enough to cover just 7 months of imports. Meanwhile, the country's current account deficit grew from 2.7 percent of GDP in 2015 to 12.4 percent in 2017. By no coincidence, the Pakistani rupee has lost nearly 20 percent of its value against the U.S. dollar since January 2017.

To be sure, many of Pakistan's financial problems predate the CPEC, as evidenced by a succession of IMF balance of payments support programs, the most recent of which ended in 2016. However, there is no doubt that Pakistan's massive borrowing from China greatly has exacerbated the problem.

A March 2017 IMF report found that CPEC loans accounted for a considerable portion of Pakistan's rising current-account deficit and external debt obligations. As a result, not only will Pakistan's economic growth fail to reach the 7 percent needed to comfortably finance its Chinese loans by 2023, the report also predicted growth would drop below 5 percent for the next several years.

By fall 2018, Pakistan's finances had deteriorated to the point where the government was again forced to request assistance from the IMF to avoid defaulting on international payments. This, by the way, prompted U.S. Secretary of State Mike Pompeo to warn the IMF against making any loans that would be used to service the Chinese debt.

As if Pakistan's dismal business environment and financial mismanagement weren't sufficient to make investors wary, add new violent unrest to the mix. Some of CPEC's projects aiming at major breakthroughs in productivity are located in dangerous places. For example, CPEC's route takes it through Baluchistan, where there are big plans to expand the small fishing village of Gwadar into a port city to rival Dubai and serve as China's opening to the Arabian Sea. Yet Baluchistan is home to a violent independence movement, the Baloch Liberation Army.

In May 2017, the Baloch killed 10 Chinese laborers working on a new road project and warned China "to vacate Baluchistan and stop plundering its resources." In response, China proposed sending Chinese troops to protect the project workers, a suggestion that Pakistan successfully rebuffed — at least for now.

What Next?

If Pakistan does get another IMF bailout, it will almost certainly be required to implement austerity measures. This in turn would threaten to destabilize the new government of cricket-star-turned-politician Imran Khan, who ran on a pledge to expand social programs to the point of creating an "Islamic Welfare State." The IMF would likely also require complete transparency on future borrowing, particularly from China, which generally prefers to keep its dealings opaque.

Khan, who didn't initiate the CPEC relationship, ordered an investigation into the terms of the various CPEC projects after his election. The inquiry found that contracts had been so poorly negotiated that they overwhelmingly favored China. For example, Pakistan reportedly guaranteed Chinese power plants annual returns as high as 17 percent over the next three decades, with the government obligated to cover shortfalls. The Khan administration has also found that many CPEC projects showed little evidence of financial viability.

While it is still too early to pass final judgment on CPEC, suffice it to say that the bloom is off the rose. At best, it may eventually deliver a portion of what was promised in terms of growth, provided the government complements the investment with the sorts of economic reforms that have thus far eluded Pakistan. At worst, CPEC could turn out to be a horrendously expensive folly that further burdens an already struggling economy.

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It's easy to see the allure of Chinese capital in countries ranging from Laos to Angola to Pakistan. The money comes without the "good government" provisions that cramp the style of leaders not accustomed to prying eyes, or the demand that local stakeholders be consulted. And, of course, it does come with the less-than-rational expectation that a little bit of the Chinese growth miracle can be imported without tears. But, as Pakistan (and other beneficiaries of Chinese capital) is learning, colonialism Chinese-style is, alas, still colonialism.

main topic: Asia